No. [redacted]

IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

156

CHARLES ORAN MENSIK and
MARY MENSIK,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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To the Honorable, The Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioners, Charles Oran Mensik and Mary Mensik, pray that a writ of certiorari be issued, to review the decision of the United States Court of Appeals for the Seventh Circuit in the above case.

JUDGMENT AND OPINION OF THE COURTS BELOW.

The judgment and opinion of the Tax Court of the United States appear in the certified record. The opinion of the United States Court of Appeals for the Seventh Circuit issued February 10, 1964. The order denying the petition for rehearing followed on March 17, 1964. The

opinion is not yet reported. The opinion of the Court of Appeals and the order above mentioned appear in the Appendix *infra* (pp. 1a-10a).

JURISDICTION

This petition is timely filed in the Supreme Court of the United States, as it is filed within ninety (90) days of the denial of the petition for rehearing in the United States Court of Appeals for the Seventh Circuit. Jurisdiction of the Court is invoked under 28 U.S.C. 1254 (1).

QUESTIONS PRESENTED

1. Does "favors received or to be received," of no determinable monetary value, or no monetary value at all, satisfy the definition of "income", as defined in the statutes and decisions of this Court?

2. Does the presumption of correctness assigned to the Commissioner's assessment of tax liability obtain conclusiveness, as interpreted in this case, or does it avail only in the absence of countervailing evidence, as interpreted by other circuits?

3. When a basic assessment is sustained only by the presumption of correctness, is not the assessment of a fraud penalty, which has its foundation in the assessment presumed correct, necessarily presumption of fraud?

4. Where a wife signer of a joint return with her spouse is assessed for a fifty per cent fraud penalty of $100,511.17, based on tax assessment in connection with the construction of a business transaction by a corporation, with which she has no connection or knowledge under the evidence, and the assessment is affirmed by the Tax Court and the Court of Appeals on presumption of correctness of the

Commissioner's assessment, and fraud is presumed and not proved by a scintilla of evidence of knowledge or willfulness or corrupt motive, is not the wife being deprived of property and branded with the stigma of fraud as an individual without due process of law and only by unreasonable presumption?

5. When the trial judge expressed incredulity at the testimony of the main witness, does not his refusal to entertain corroborating evidence, on the stated ground that it would be merely cumulative, necessarily assign the same incredulity to evidence he has never considered, in violation of due process?

6. Whether a jeopardy assessment of the original sum of $547,967.55 and an addition to tax for fraud in the amount of $273,983.78 was reduced more than $500,000.00 (over 60% of original assessment of tax and fraud penalties) by stipulation and concession of the respondent Commissioner, and further reduced by decision of the Tax Court to $201,022.33 of tax and $100,511.17 in fraud penalties, and the determination that these lesser amounts due is based upon a claimed presumption of correctness and regularity in the original determination of tax by the Commissioner, and conjecture that money loaned by a corporation to a third party might subsequently inure to the benefit of one of the petitioners, was it not error and denial of due process of law for the Tax Court to arbitrarily reject a petition for rehearing, supported by adequate affidavits showing that the crucial loans were not and could not be income or economic gain to either petitioner?

STATUTES INVOLVED.

Internal Revenue Code of 1954:

Sec. 61. Gross income defined.

(a) *Several Definitions.* — Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, and similar items;

(2) Gross income derived from business;

(3) Gains derived from dealing in property;

• • •

(26 U.S.C., 1958 ed., Sec. 61.)

Sec. 6653. Failure to pay tax

(a) *Negligence or Intentional Disregard of Rules and Regulations With Respect to Income or Gift Taxes.* • • •

(b) *Fraud.*—If any part of the underpayment (as defined in subsection (c)) of the tax required to be shown on a return is due to fraud, there shall be added to the tax an amount equal to 50% of the underpayment. In the case of income taxes and gift taxes, this amount shall be in lieu of any amount determined under subsection (a).

• • •

(26 U.S.C., 1958 ed., Sec. 6653.)

STATEMENT OF THE CASE.

This civil proceeding is a specific items case involving some nine issues and did not involve any theory of net worth in its presentation of proof. This case was initiated in June of 1957 less than 90 days after Petitioners filed their 1956 income tax return at which time taxpay-

ers made all their records available to the Internal Revenue Service. On June 17, 1958 the Respondent Commissioner issued a jeopardy assessment in the total amount of $821,951.33, including additions to tax in the amount of $547,967.55 and fraud penalties of $273,983.78 for the calendar year of 1956. On or about the same day, the Internal Revenue Service served notice of levies on approximately 200 persons predicated upon the aforesaid Jeopardy Assessment thus advising approximately 200 persons including corporations holding property and funds belonging to petitioner that the male taxpayer not only owed Federal Income tax but further the Internal Revenue Service was taking the most drastic course possible to force payment because the tax was in jeopardy. On September 14, 1958 petitioners filed a petition in the Tax Court of the United States for a redetermination of the deficiency, as set forth by the Commissioner of Internal Revenue in his notice of deficiency, and during the course of proceedings prior to trial the Respondent Commissioner conceded errors and inaccuracies in the deficiency assessment of more than 60 per cent of the amounts assessed, amounting to errors of more than $500,000.00 of the asserted tax and penalties. On June 14, 1959, the date of trial, respondent filed a motion for leave to file an amendment to answer, changing [redacted] of the case, as well as the amounts of deficiency, to which petitioners filed objections. The Tax Court overruled petitioners' objections, allowed the amendment to deficiency, and proceeded immediately to trial. The case was heard and the Tax Court entered its decision on January 16, 1962. The Tax Court found a tax deficiency in the amount of $201,022.33 for the taxable year 1956, and an addition to tax for fraud in the amount of $100,511.17. On January 30, 1962 peti-

tioners filed a motion for rehearing (Pet. App. p. 113), which the Tax Court denied on August 22, 1962.

Petitioners filed a petition for review in the United States Court of Appeals for the Seventh Circuit on March 27, 1963. The matter was heard and the Circuit Court entered its decision on February 10, 1964, affirming the decision of the Tax Court of the United States. Petitioners filed a timely petition for rehearing which was denied by the Court of Appeals on March 17, 1964.

When petitioners filed proceedings in the Tax Court of the United States on September 11, 1958, the parties entered into a series of conferences to arrive at stipulations. During the course of these conferences, the Respondent Commissioner agreed to stipulations (Pet. App., pp. 64-65) conceding inaccuracies amounting to well more than half of the amount of the tax assessment, and abandoned more than $300,000.00 of the original assessment of tax in the notice of deficiency. (Pet. App. p. 65).

Preliminary to the taking of evidence in the Tax Court, on the consideration of procedure to be followed, the Respondent was informed that it was the intention of the petitioners to subpoena as a witness formed State Auditor Orville E. Hodge, who was then in prison. After discussion of this and other matters, and upon consideration of the representation by respondent's counsel that the receipt of loans in the sum of $176,312.50 by Hodge would not be contested, the petitioners abandoned their stated proposal to request the issuance of a *writ of habeas corpus ad testificandum*, to secure the presence of Hodge. On the date of trial, the Respondent filed an amended answer which changed its original answer (Pet. App., p. 21), which had asserted the *amount* of specific item #3 as being $176,312.50 and the *source* as "loan transactions" between Or-

ville E. Hodge and the Melvin Building Corporation. The new answer (Pet. App., p. 27) changed the *amount* of this specific item to $206,330.56, and now asserted the *source* to be the "measure" of an alleged payment for a remodeling job by Melvin Building Corporation for City Savings Association, a mutual association, of which the male petitioner was an officer and director. Petitioners filed objection (Pet. App., p. 28) to the amended answer, and the Tax Court denied the objection, allowed respondent to amend the answer, and simultaneously ordered trial to commence. This is a "specific items" case and Petitioners, having marshalled their evidence and witnesses to meet Respondent's original "theory of the case", were taken by surprise when the Tax Court allowed the Respondent to change both the *amount* and *source* of this item.

It was not until after the Court's decision that Petitioners learned that the Tax Court had adopted a theory of the case which the Respondent had led Petitioners to believe would not be in issue, and a petition for rehearing was filed immediately, with annexed affidavits by the attorneys for the Petitioners and by Orville E. Hodge. (See Exs. 4 & 5, Pet. App. pp. 129-130). These affidavits demonstrate that the Petitioners were misled by government counsel into not calling Hodge as a witness.

It is not contested that during the pertinent year, 1956, the male Petitioner was an officer and employee of City Savings Association which offered, as a part of its service to business men and to the general public, the use of its facilities for the cashing of checks in substantial amounts in connection with real estate closings, loans and other transactions, wherein the Association was not a party to the transaction, and no funds of the Association were involved. The record is clear that the male Petitioner rendered such service to the parties involved in this

transaction at issue as item #1, the *lender* being Melvin Building Corporation and the *borrower* being Orville E. Hodge. Petitioner acted in the usual manner as an escrow agent or broker would act for such transactions, and the exhibits documents reflect that the Melvin Building Corporation, upon its delivery of $176,312.50, represented by its execution of 3 checks (Ex. 9, 10, 11, pp. 135-137, Pet. App.), received the corresponding promissory notes executed by Orville E. Hodge, acknowledging his loan from Melvin Building Corporation. (Exs. 6, 7, 8, pp. 132-134 Pet. App.) Exhibit No. 9, a check dated March 12, 1956 in the amount of $76,312.50 was made out to Orville E. Hodge, and this exhibit shows his endorsement and deposit in his bank at Granite City, Illinois two (2) days later, in the regular course of business.

The testimonial evidence further disclosed that Hodge had requested the remaining $100,000.00 in cash. This testimonial evidence was corroborated by documentary evidence, in the form of two (2) $50,000.00 promissory notes made to Melvin Building Corporation and executed by Hodge. Hodge's affidavit, filed in support of the motion for rehearing, acknowledge the receipt of the full $176,312.50, and reaffirmed the aforesaid testimonial and documentary evidence.

The Tax Court in its decision and findings, asserted fraud penalties only in connection with the single item of $176,312.50, and made no such separate findings in connection with the other two items of fraud, asserted by the Commissioner. (Pet. App. pg. 110). It is to be noted that the Court of Appeals, in its decision (A. p. 9a) *infra*, characterized such finding of fraud as being based upon "consideration of the record as a whole", thus misapprehending the decision of the Tax Court, and further misapprehending that petitioners' appeal was based upon the

failure of the record to support the receipt of this single item by petitioners, and the valid contradiction of the presumption of correctness initially attaching the Commissioner's assessment, which the respondent admitted to be in error, both by amended answer and by *stipulation*.

The uncertainty of the Tax Court is evident from the very language of its inconclusive findings. Further these factors and the documentary proof to the contrary notwithstanding, the Tax Court held in regard to the alleged deficiency of $176,312.50 (by amended answer increased to $206,330.56) as follows:

> "Held, further, that petitioner has failed to prove that the income so received was in a lesser amount than determined by respondent in his determination of deficiency. Held, further, that the respondent has failed to carry his burden of proving that the income so received by petitioner was in an amount greater than determined by him in his determination of deficiency." (Pet. App. pg. 30)

And, again:

> "With respect to the first of the issues stated, the respondent has made no concession, but to the contrary, now claims, by amended answer, that the amount in issue should be increased from $176,312.50, as originally determined, to $206,330.50. There is, of course, no presumption of correctness as to the additional amount now claimed, but *as to $176,312.50* covered in respondent's determination of deficiency, *the presumption of correctness continues.*" (App. 66) (Emphasis supplied.)

And, further:

> "Also, we are persuaded and convinced that they were made with the deliberate purpose of providing funds for the payments made to him by Melvin, whether they were intended for him *or* for Hodge, or whether they

came to rest with him or were passed on to Hodge. What the arrangement *was* between petitioner and Hodge, *we do not know*. It *could be* that a pay-off to Hodge for favors received or to be received by petitioner or his wholly-owned loan companies was made. *Whatever they were*, and to the extent they did occur, we are satisfied that they were advisedly arranged for and made by petitioner, and *there is no evidence of record* which persuades us that there was any intention that such payments which did reach Hodge, *if any*, were to be repaid." (App. 94) (Emphasis supplied.)

Aside from the foregoing documentary proof that trial Judge did not regard as reliable the male petitioner's testimony and even though the Respondent introduced no evidence or documents to contradict taxpayer's position the Tax Court held that the "presumption of correctness" supported the assessment. This situation obtained as to the other items in issue notwithstanding the proof both testimonial and documentary, introduced by Petitioners as to each and every issue. Thus, the Tax Court found that, on the presumption of correctness, the petitioners were to be assessed $176,312.50. Though the Commissioner alleged fraud in three items, one for the $176,312.50, another of $10,000.00, and a third in the amount of $6,800.00 (Pet. App. pg. 110), the Tax Court found fraud only in the item of $176,312.50 (Pet. App. pg. 111-113). The Court of Appeals for the Seventh Circuit held that the "record as a whole" supported the finding of fraud by the Tax Court. (Ap. p. 7a) *infra*. This was contrary to the finding of the Tax Court, which made the specific item of $176,312.50 the sole basis for its finding of fraud.

REASONS FOR GRANTING THE WRIT.

I.

The decision of the Tax Court, endorsed by the affirmance of the Court of Appeals, that "favors received or to be received" of no determinable monetary value, or no monetary value at all, satisfies the definition of "income", is contrary to the statute and in conflict with applicable decisions of this Court.

The Tax Court found:

> "• • • What the arrangement was between petitioner and Hodge, *we do not know*. It could be that a pay-off to Hodge, *for favors* received or *to be received* by petitioner or his wholly-owned loan companies was made. Whatever they were, and to the extent they did occur, we are satisfied that they were advisedly arranged for and made by petitioner, • • • (Pet. App. pg. 94) (Emphasis supplied.)

To sustain a finding of the receipt of taxable income it is not enough for a Tax Court to say it does in its opinion that this $176,312.50, which Hodge received, could be for "Prior Favors" received or "to be" received from Hodge by the Petitioners or the loan associations in which they held shares. There is here no measurable economic gain that can be ascertained by the receipt of "favors" and the Tax Court erred in its finding that such amount constituted the receipt of "taxable income" to petitioners. We respectfully submit that to assess petitioners with the obligation to pay additions to tax on the basis of such a finding would deprive petitioners of property in violation of their constitutional rights of Due Process of Law.

Analyzing this uncertain decision of the Tax Court, the most concrete thing said is that the Tax Court considered that this might have been a "pay-off" to Hodge for favors received or to be received. It is our submission that such an interpretation of "income", under the Sixteenth Amendment and under 26 U. S. C., Sec. 61, is contrary to law and a perversion of both the Constitution and the Statute. The Sixteenth Amendment is a grant of power for the taxation of income. Under it, that may not be taxed which is not "income". *Eisner* v. *Macomber*, 252 U. S. 189; *M. E. Blatt Co.* v. *United States*, 305 U. S. 267. This Court also found in *Helvering* v. *Stuart*, 317 U. S. 154, that:

> "Economic gain realizable by the taxpayer is necessary to produce a taxable income under our statutory scheme."

Further, in *Merchants L. & T. Co.* v. *Smietanka*, 255 U. S. 509, this Court said at p. 519:

> "In determining the definition of the word 'income' thus arrived at, this Court has consistently refused to enter into the refinement of lexicographers or economists, and as a proof, in the definitions quoted, what it believes to be the commonly understood meaning of the term which must have been in the minds of the people when they adopted the Sixteenth Amendment to the Constitution."

The Tax Court by its own language, see (Pet. App. pg. 94) • • • "We do not know what the full and true story is with respect to the payments by Melvin to petitioner in 1956." • • • "What the arrangement was between petitioner and Hodge we do not know." • • • "Whatever they were, and to the extent that they did occur • • •" (Pet. App. pg. 95) • • • "Frankly, considering the state of the record, we do not know what the truth is" • • •.

clearly demonstrates its own confusion, conjecture and uncertainty. The decision of the trial court, affirmed by the Court of Appeals, has here resulted in a crushing assessment of tax and penalties against these petitioners placing them in financial jeopardy to pay more than $300,000.00 in a proceeding that has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

On the basis of the statutes, and on the cases decided by this Court, including those adverted to hereinbefore, we respectfully submit that the decision of the Tax Court in this case, as approved by the Court of Appeals for the Seventh Circuit, constitutes a decision on a federal question in a way in direct conflict with the applicable decisions of this Court, and, on that account, certiorari should be granted.

II.

In this case, the presumption of correctness assigned to the Commissioner's assessment of tax liability was the only factor that supported the decision, even though there was contravening evidence adduced as to each item comprising the assessment. This decision is in conflict with decisions of other Court of Appeal on the same matter.

The assessment filed herein is comprised of eight items in issue. As to the three most substantial of them, the Tax Court found as follows:

> (1) "Held, further, that petitioner has failed to prove that the income so received was in a lesser amount than determined by Respondent in his determination of deficiency. Held, further, that the Respondent has failed to carry his burden of proving that the income so received by Petitioner was in an amount greater than determined by him in his determination of deficiency." (Pet. App. pg 39)

(2) "The Respondent determined that by reason of the receipt of the $10,000.00 in 1956, petitioner realized income in that amount. Held, that petitioner has failed to show by convincing or persuasive proof that the Respondent erred in his determination." (Pet. App. pg. 31)

(3) "Held, that petitioner has failed to prove that the Respondent erred." (Pet. App. pg. 32)

As to each of these items, and as to all the others, the petitioners introduced proof, both testimonial and documentary. Notwithstanding the proof introduced, this Court will see, as demonstrated herein, that the original assessment found its support in the Tax Court merely on the presumption of correctness which attached to the notice of deficiency made by the Commissioner.

This record is devoid of any showing that the petitioners received taxable income, *even by constructive receipt*, in connection with the checks issued by the Melvin Building Corporation in the amount of $176,312.50, which Orville E. Hodge received, and acknowledged by his execution of corresponding promissory notes, introduced in the trial of this case below Ex. Nos. 6, 7, & 8, (Pet. App. pp. 132-134)[1] There was no showing by Respondent that revenue agents were able to demonstrate through their analysis of petitioners' bank accounts and flow of funds that *any part* of this amount was received by the taxpayer or his wife. The record is clear that petitioners did not receive this money.

[1] The Commissioner of Internal Revenue has assessed Orville E. Hodge for the full amount to the penny ($176,312.50 as taxable income to him for this same year, and has disallowed the lender of the money, Melvin Building Corporation, a "bad debt" deduction for the identical amount loaned to Hodge for this same year. There is no mistaking this item because the amount is precisely identical in the case of each assessment and corrected assessment.

It is fundamental that the Tax Court must give proper credit to unimpeached uncontradicted evidence and may not arbitrarily disregard such testimony or documents in violation of recognized judicial standards and procedures and due processes inherent in our laws.

It is our respectful submission that such a determination is in conflict with other circuits, including the following:

> "While there is a presumption that the action of the Commissioner is correct, that presumption disappears when evidence is introduced to overcome it." *Kentucky Trust Co.* v. *Glenn*, 6 Cir., 217 F. 2d 452-465.

See also *Collings' Estate* v. *United States*, W. D. Ky., 138 F. Supp. 837-841; *Manchester Board & Paper Co.* v. *C.I.R.*, 4 Cir., 89 F. 2d 313; *Woodward* v. *United States*, 106 F. Supp. 14, aff'd., 8 Cir., 208 F. 2d 893.

III.

In this cause, the basic assessment was sustained only by a presumption of correctness attached to the notice of deficiency, notwithstanding the admitted error in excess of $500,000.00 (over 60% of original assessment of tax and fraud penalties). The Court relied only on the presumption of correctness. On that basic assessment, presumed correct, a fraud penalty was further assessed. It is our submission that this constitutes presumption of fraud, contrary to applicable decisions of this Court, and in conflict with the decisions of other Courts of Appeal on the same subject.

We submit to the Court that the burden of proof, being an understatement of income motivated by fraud, was, in accordance with general decisions, incumbent upon the Commissioner-Respondent. But, before it can be said that

an understatement was fraudulent, the understatement itself must be proved, and not presumed. Presuming one of the vital elements of the burden that was the Commissioner's necessarily constitutes a *presumption* of fraud.

The fraud penalty was added by the Tax Court to the assessment of tax against the petitioners by reason of failure to report a sum that the Hodge affidavit (Pet. App. pg. 127), and the Commissioner's Notice of Deficiency to Hodge show have been assessed as taxable income against him. Undeniably the record shows that Melvin Building Corporation paid tax on the $176,312.50 when its claim of deduction in its 1956 income tax return (see Trial Exhibit S) for Hodge's bad debt was disallowed. There is no mistaking the fund for the figure is the same in the case of each assessment, and corrected assessment.

This demonstrates beyond argument that the disclosure by Melvin of the amounts in its 1956 income tax return claiming deduction for Hodge's bad debt, the delivery of notes by Hodge to Melvin for the amount, the book entries by Melvin concerning the loans and the ready testimony of all parties concerned, dispel any claim of concealment. There was rather an abundant disclosure which led to three assessments of tax on the same item in three investigations of the parties. Even if all of these assessments are to be treated initially as presumably correct, unreasonable presumption fails, when contradicted validly, or when it departs from reason and experience. (See *Tot* v. *United States*, 319 U.S. 463, 467-469; 87 L. Ed. 1519, 1524, 1525.)

We respectfully submit that the decision of the Tax Court, affirmed by the Court of Appeals for the Seventh Circuit, is contrary to this Court's decision in *Vitelli & Son* v. *United States*, 250 U.S. 355, which case is a land-

mark decision that fraud must be found, without reference to any presumption of law or fact.

We further submit that the decision of the Tax Court and of the Court of Appeals in this cause is contrary to the holding of the Sixth Circuit in *Hawkins* v. *C.I.R.*, 234 F. 2d 359, 360, and to the holding of the Third Circuit in *Valetti* v. *C.I.R.*, 260 F. 2d 185, 188.

This Court's particular attention is directed to a comparison between this case and *Goldberg* v. *C.I.R.*, 5 Cir., 239 F. 2d 316.

In the *Goldberg* case, the Fifth Circuit restated some of the Tax Court's findings, which reflect a definite similarity with the findings here:

> "As to the legal expense, the Tax Court disallowed the deduction and said. 'For aught the record shows, some, if not all, of the legal expenses involved might very well have been and probably were, incurred in defending criminal actions against petitioner or his employees, or securing their release from custody, or in regaining possession of slot machines which had been confiscated.' These inferences were made by the Tax Court in sustaining the tax deficiencies where the petitioner had the burden of proof and the Commissioner had the benefit of a presumption. They can hardly be regarded as showing or tending to show a specific fraudulent intent to evade income taxes."
>
> *Goldberg* v. *C.I.R.*, 239 F. 2d 316, 321.

In the instant case, the Tax Court found:

> "• • • they were made with the deliberate purpose of providing funds for the payments made to him by Melvin, whether they were intended for him or for Hodge, or whether they came to rest with him or were passed on to Hodge. What the arrangement was between petitioner and Hodge, we do not know. It could

be that a pay-off to Hodge for favors received or to be received by petitioner or his wholly-owned loan companies was made. Whatever they were, and to the extent they did occur, • • •" (Pet. App. pg. 94).

The Tax Court further found (Pet. App. pg. 112):

• • • "Accordingly we are satisfied and convinced that *if any* of the funds so received by petitioner from Melvin were in turn paid over to Hodge with any understanding between him and Hodge that repayment was to be made, it was petitioner's purpose and intent that in whole or substantial part he *would be* the ultimate recipient. And insofar as the funds purportedly loaned to petitioner represented funds diverted from City Savings under the guise of payments for the remodeling of its building the same is true as with respect to the purported loans to Hodge • • •". (Emphasis supplied.)

It is respectfully submitted that this language of the Tax Court in its decision which was affirmed by the Court of Appeals "in all respects," clearly demonstrates that Petitioners are being assessed additions to tax and fraud penalties in violation of Due Process of Law by a Court which finds;

1. That it is not certain of the amount involved on construction work by a corporation;
2. That it is not certain who received the money;
3. That holds; Even if the Petitioners did not receive the money, one of them must have intended to become its ultimate recipient.

IV

The assessment of a fraud penalty against the wife signer, who under this record had no connection with, or knowledge of, any of the transactions with which the evidence was concerned, is in conflict with the decision of other Courts of Appeals on the same matter.

In this cause, Mrs. Mary Mensik filed a joint return with her husband, Charles Oran Mensik. She was assessed with a 50% fraud penalty of $100,511.17, based on a tax assessment in connection with the construction of a business transaction by a corporation with which she had no connection or knowledge under the evidence. This assessment against Mrs. Mensik was affirmed by the Tax Court and the Court of Appeals for the Seventh Circuit on a presumption of correctness of the Commissioner's assessment, as has been discussed hereinbefore. Not one scintilla of evidence of knowledge of these transactions, much less willfulness or corrupt motive, finds support in the evidence as to Mrs. Mensik. It is our submission that she has been deprived of property, and branded with the stigma of fraud as an individual, without Due Process of Law and only by an unreasonable presumption.

There is no mention of the conduct of Mrs. Mensik in the record which is completely bare of evidence of any kind or nature offered by the Respondent in connection with the burden of proof, which is a requirement to be satisfied by the Respondent to sustain the imposition of fraud penalties against this petitioner.

The Revenue Acts as passed by the Congress apply to individuals throughout the nation and further the separate State Laws vary in the matter of property rights of a spouse. It is respectfully submitted that this issue presents a matter of vital importance in the public interest and when a wife signs a joint return where fraud penalties

are subsequently asserted because of the conduct of a husband in connection with his receipt of income even if it be unknown to her, an unfair obligation of payment places such person in complete financial jeopardy. Further, upon divorce or in the event of the death of her spouse she, without fault, is faced with crushing penalties and obligations to pay amounts impossible for her to meet. Should such divorced person or widow remarry her new spouse could become subject to tremendous financial obligations not contemplated by him at the time of such marriage. We respectfully submit this constitutes an important question in Federal Law, which has not been, but should be, settled by this Court.

There is absolutely no evidence or presumption to support imposition of fraud penalty against Mary Mensik. The Commissioner-Respondent did not prove or *state* one iota or scintilla of fact that would indicate his intention to contend her conduct was fraudulent. (See *Cirillo* v. *C.I.R.*, 314 F. 2d 478, 484.)

The original assessment having been upheld by a presumption of correctness, and the female petitioner's [Mrs. Mary Mensik's] liability being created by a similar presumption, offends against basic legal concepts of the requirements for assertions of fraud penalties and established standards of proof in derogation of Petitioner's constitutional rights of Due Process of Law.

V.

The main witness in this cause was the male petitioner. The trial Judge expressed incredulity at his testimony, and then refused to entertain corroborating evidence, on the stated ground that it would be merely cumulative.

Hodge's testimony and affidavit (Pet. App. pp. 121-122, 127-128) shows unequivocally that he received loans from Melvin in the amounts in debate, and described the manner in which each amount, comprising the total sum of $176,312.50 was received by him.[2]

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[2] See transcript of testimony of Orville E. Hodge, taken at Illinois State Penitentiary, Menard Branch, Menard, Illinois, by agents of the Internal Revenue Service, at a time when neither the petitioners nor their attorneys were present (Pet. App. pp. 121-122):

"Q. How were you able to acquire so much money from and through Mr. Mensik, Mr. Hodge, during the periods we have discussed?

"A. My only answer is that I had the collateral to back up a loan.

"Q. Could these so-called loans have represented a consideration for any favor that you have granted Mr. Mensik or his association?

"A. I never gave Mr. Mensik any more favors than I gave any other loan Associations in Chicago or the State of Illinois.

"Q. He did, however, get two charters for stock—

"A. He didn't get these from me directly. He got them from the committee.

"Q. You approved them?

"A. I didn't- the committee did.

"Q. As State Auditor, didn't you have to approve them?

"A. I didn't approve them. I signed them after their approval."

Also, see Affidavit of Orville E. Hodge, annexed to Petitioner's petition for rehearing in the Tax Court. (Pet. App. pp. 127-128)

"That, in the course of building the Esquire Hotel in Florida, affiant borrowed $176,312.50 from Melvin Building Corporation. This amount was used by your affiant for such purpose. This money was received from the Melvin Building Corporation and, for this amount, your affiant signed certain promissory notes. Affiant further states that he intended to pay this money back to Melvin Building Corporation within a year. Affiant had also borrowed $200,000.00 from City Savings Association in Chicago, Illinois, and affi-

The Tax Court Judge, concurred in by the Seventh Circuit Court of Appeals, viewed this aspect of the case as follows: (See comment of Tax Court Judge on denial of rehearing (P. 36, Tr. Aug. 22, 1962).

> "The Court dealt with the issue in that posture and the Court said very plainly that on the record in this case and on the evidence, the *answer* would be the same, whether or not Hodge received the money as a *bona fide loan or* whether he *didn't* receive it. And the Court is still of the view that the record is ample and adequate to support and sustain the findings he made in the decision, and that if Hodge were called as petitioner now desires, to testify that he did receive the money as a loan; that would not change the disposition of the case, and I think that the Opinion amply shows that.
>
> "The situation being as it is, the motion for rehearing is denied."
>
> "All right, the ruling has been made on the motion, and we will stand adjourned." (Emphasis supplied)

(Continued)

ant had given as security for this money a first mortgage on the Esquire Hotel. Your affiant states that, if he were unable to pay back the $176,312.50 to Melvin Building Corporation within the year, affiant intended to issue a second mortgage to Melvin Building Corporation on the Esquire Hotel in Miami, Florida. Affiant states that the said Hotel, in affiant's opinion, was worth at least $700,000.00, and that, at a forced sale, and under peculiar circumstances, it was sold for $575,000.00. Affiant felt that a total mortgage of the amount of $376,312.50 was an amount well within the actual value of said property.

"Your affiant regarded the loan from Melvin Building Corporation as a pure business deal, and your affiant, in his private and official capacities, did no favors for C. Oran Mensik in return for the loan of this money or any other monies."

It does violence to reason for the Tax Court to say as it did: "The answer would be the same whether or not Hodge received the money as a bona fide loan or whether he didn't receive it." (Emphasis supplied) Logic dictates that the answer could not be the same because the bona-fide Loan from Melvin Building Corporation to Hodge could not be receipt of taxable income by petitioners. Due Process is an absolute constitutional guarantee and the refusal of the trial court to allow Petitioners to call this vital witness Hodge, to acknowledge that he received the money, was an abuse of its discretion and a clear violation of Petitioner's right of Due Process of Law.

We respectfully submit that it is a necessary deduction from the action of the trial court that he assigned incredulity to evidence he refused to consider, in violation of Due Process of Law and in violation of his clear obligation to weigh the evidence.

VI.

Preliminary to the taking of evidence in this case, on the consideration of procedure to be followed, the Court was informed that it was the intention of the petitioners to subpoena as a witness a former State Auditor Hodge, who was then in prison. After discussion of this and other matters with government counsel, and upon the representation by government counsel that the receipt of loans in the sum of $176,312.50 by Hodge would not be contested, the petitioners abandoned their thought of requesting subpoena for Hodge.

It was not until after the Court's decision that petitioners learned that the Tax Court had adopted a theory of the case which the Respondent had led petitioners to believe would not be in issue, and a petition for rehear-

ing was filed immediately, with annexed affidavits by the attorneys for the petitioners and by Orville E. Hodge. (See Exhibits 4 and 5, Pet. App. pp. 129-130). These affidavits definitely demonstrate that the petitioners were misled by government counsel into not calling Hodge as a witness.

Hodge's affidavit (Pet. App. pg. 127), as annexed to Petitioners' petition for rehearing, shows unequivocally that he received loans from Melvin in the exact amount in issue, and described the manner in which each amount comprising the total sum of $176,312.50 was received by him. In the view taken by the Tax Court Judge of this aspect of the case Hodge's testimony, in accordance with his affidavit, would have been *crucial testimony*. Hodge would have been available for cross-examination. The opportunity for the Judge to consider his manner of testimony, his memory, and his general demeanor, factors considered so important in the decision of the lower court, was a vital factor, to which the Tax Court Judge refused to expose himself. The Tax Court's failure to grant rehearing after decision, in the face of compelling proof by affidavits that justice required such motion be granted, was not a mere exercise of discretion, but an unfounded abuse of discretion.

Further corroboration by documentary evidence was introduced in the form of two (2) promissory notes executed by Hodge to Melvin, each in the amount of $50,000.00 in receipt of $100,000.00 by Hodge (Pet. App. pp. 133, 134, Ex. 7 and 8). This amount together with the check to Hodge from Melvin for $76,312.50 made a total of $176,312.50, the full amount of this item.

The complete disregard of evidence by the Tax Court includes a total failure to explain any conclusion it reached, if any, concerning the check of Melvin for $76,312.50 payable to Hodge and endorsed by him and deposited in his own bank at Granite City, Illinois, and which was one of the loans comprising the total of $176,312.50 loaned by Melvin to Hodge (Pet. App. pg. 135, Exhibit #9). Apparently since the Tax Court could not rationalize this item into its findings and conclusions, it ignored it.

We submit that such a determination and preclusion of evidence on behalf of these Petitioners so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

CONCLUSION.

The decision of the Court below has decided federal questions in conflict with decisions of other United States Circuit Courts of Appeal and in conflict with applicable decisions of this Court and has so far departed from the accepted and usual course of judicial proceedings and sanctioned such departures by the Tax Court of the United States in its trial of this case as to call for an exercise of this Court's power of supervision. For the reasons stated, it is respectfully submitted that this petition for writ of certiorari should be granted.

Respectfully submitted,

KENNETH T. JAMES,
Attorney for Petitioners.

APPENDIX A

IN THE

UNITED STATES COURT OF APPEALS

FOR THE SEVENTH CIRCUIT

No. 14167 SEPTEMBER TERM, 1963—JANUARY SESSION, 1964

CHARLES ORAN MENSIK and MARY MENSIK,
Petitioners,
v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition to Review the Decision of the Tax Court of the United States.

February 10, 1964

Before HASTINGS, *Chief Judge*, SCHNACKENBERG and SWYGERT, *Circuit Judges*.

HASTINGS, *Chief Judge*. This case is before us on petition of Charles Oran Mensik and Mary Mensik, his wife, for review of a decision of the Tax Court of the United States. *Mensik v. Commissioner of Internal Revenue*, 37 T. C. 703 (1962).

The Commissioner of Internal Revenue, respondent, assessed petitioners a tax deficiency of $547,907.55 for the taxable year ending December 31, 1956, and a fifty per cent

penalty for fraud of $273,983.78, as provided in Section 6653(b) of the Internal Revenue Code of 1954, 26 U.S.C.A. §1221 (1958 ed.).[1]

The decision of the Tax Court ordered petitioners to pay $201,022.33 income tax deficiency and $100,511.17 fraud penalty.

The Tax Court's preface to its opinion concisely states the case by setting out the following general findings of fact and holdings:

> "1. Petitioner [Charles Oran Mensik] as managing officer, president, and chairman of the board of directors of the City Savings Association, employed Melvin Building Corporation to do remodeling of the building of City Savings and in payment therefor caused City Savings to make a gross overpayment for the work actually done, which overpayment was advisedly arranged by petitioner. At or near various dates on which the final payments were being made by City Savings to Melvin, petitioner arranged with Melvin to deliver to him various substantial sums of money as purported loans to him and one Orville Hodge, then State auditor for the State of Illinois. The respondent in his determination of deficiency determined that to the extent of $176,312.50 the moneys so paid over to petitioner constituted income to him. By amended answer, it is his claim that this amount should be increased to $206,330.56. *Held*, that some part, if not all, of the overpayment made by City Savings to Melvin was thereafter paid over by Melvin to petitioner and was income to him. *Held, further*, that petitioner has failed to prove that the income so received was in a

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[1] "§6653. Failure to pay tax

* * *

"(b) Fraud.—If any part of any underpayment * * * of tax required to be shown on a return is due to fraud, there shall be added to the tax an amount equal to 50 per cent of the underpayment. * * *"

lesser amount than determined by respondent in his determination of deficiency. *Held, further*, that the respondent has failed to carry his burden of proving that the income so received by petitioner was in an amount greater than determined by him in his determination of deficiency.

"2. In October of 1954, Melvin Building Corporation entered into a contract with petitioner's sister for the purchase of 13 lots on West Jackson Boulevard in Chicago, and made a substantial cash payment on the purchase price. The entries on its books reflected only the purchase of lots 2 to 13, inclusive. Early in 1956, Melvin began construction of a building on some or all of the lots including lot 1, and received a construction loan from City Savings therefor. On May 25, 1956, after substantial amounts had been advanced on the loan and the construction was under way, Melvin issued a check for $10,000 to petitioner and entered the payment on its books as payment for lot 1. On March 11, 1957, petitioner, by check, made a payment of $10,000 to Melvin, which check Melvin credited to its notes receivable account. It is petitioner's testimony and claim that the $10,000 paid in March of 1957 was a repayment of the $10,000 received in May of 1956, the repayment being made after discovery that Melvin already owned lot 1. No change in the application of the payment of $10,000 in May of 1956 or in receipt of $10,000 in March of 1957 has ever been made on Melvin's books. The respondent determined that by reason of the receipt of the $10,000 in 1956, petitioner realized income in that amount. *Held*, that petitioner has failed to show by convincing or persuasive proof that the respondent erred in his determination.

"3. In 1956, petitioner caused a check to be drawn on a bank account of City Savings Association for $6,800. The payee shown was Commercial Broadcasters and the basis for the drawing of the check was an invoice made out on a form of Commercial Broad-

casters. The invoice was not the invoice of Commercial Broadcasters and Commercial Broadcasters never received the check. Commercial Broadcasters did not arrange a program or programs such as were described on the bogus invoice. The respondent determined that by reason of the $6,800 payment by City Savings, petitioner realized income in that amount. *Held*, that petitioner has failed to prove that the respondent erred.

"4. Through his relations with City Savings and with Melvin and other institutions with which he occupied dominant positions, petitioner regularly carried on varied business operations, which included the purchase and sale of real estate. *Held*, that the parcels of real estate sold by petitioner in 1956 were sold to customers in the ordinary course of his business, and that the gain therefrom was not capital gain, but ordinary income. *Held, further*, that the income derived from the purchase of real estate tax certificates and their subsequent redemption was ordinary income.

"5. During 1956 petitioner, in the course of his business, sold insurance policies to his employees, to employees of City Savings, and to relatives and friends, on which sales he waived his commissions in favor of the purchasers. The respondent determined that petitioner realized income in the amount of the commissions waived. *Held*, that respondent did not err in his determination.

"6. In June of 1955, petitioner organized the First Guarantee Savings Association, of which he owned 98.8 percent of its stock, and the Chicago Guarantee Savings Association, of which he owned 98.6 percent of the stock. On July 1, 1955, he executed written instruments with each of the associations, reciting that he agreed to spend $55,000 in advertising each such association during the period July 1, 1955, and June 30, 1956. In each instrument it was recited that the association would recommend and give all of the insurance of its members and its own to petitioner for a

period of 5 years, and for an additional 5 years, if $100,000 in commissions was not received by petitioner during the first 5 years. Petitioner expended $17,295.14 in 1955 and $32,076.14 in 1956 for advertising of First Guarantee, and $18,374.84 in 1955 and $36,284.84 in 1956 for advertising Chicago Guarantee. In 1956 he deducted as advertising expenses of his operations carried on under the name of City Insurance Agency, $8,951.93, which was the same in amount as the sum of $5,139.81 received in 1956 in the form of commissions on insurance business originating with First Guarantee and $3,812.12 on business originating with Chicago Guarantee. *Held*, that the amounts expended by petitioner in 1955 and 1956 in advertising the two savings associations represented capital contributions by him to the associations.

"7. In June of 1955, when Chicago Guarantee Savings Association was organized, petitioner paid $9,000 as rent for 20 months for space to be occupied by the association, for $2,000 of which he was reimbursed. In reporting his income for 1955, petitioner deducted as rent $2,700 of the $7,000 net balance, and in his 1956 return deducted the remaining $4,300. *Held*, that the $7,000 so expended by petitioner in June of 1955 was a capital contribution by him to Chicago Guarantee.

"8. In September of 1956, petitioner received premium refunds of $6,166.42 from the insurer of the buildings of First Guarantee Savings Association and Chicago Guarantee Savings Association, this insurance having been sold by petitioner to the associations in the course of his personal business operations. The amounts so received by petitioner were retained by him and have never been paid over to the said associations. *Held*, that the respondent did not err in determining that petitioner realized income in 1956 in the amount of insurance premiums so refunded and received by him." 37 T. C. at 703-705.

The Tax Court then follows with nineteen pages of particularized findings of fact in support of the above general findings. *Id.* at 706-724. These findings are incorporated in this opinion by reference thereto.

Reference is further made to the Tax Court's extended opinion by Judge Turner. *Id.* at 724-754.

On appeal, these findings of the Tax Court must stand unless shown to be clearly erroneous. *Commissioner* v. *Duberstein*, 363 U.S. 278, 291 (1960); *Interstate Drop Forge Company* v. *Commissioner of Internal Revenue*, 7 Cir., ... F. 2d ..... (January 7, 1964).

Petitioners contend "that the Tax Court's findings of fact and law constitute erroneous legal conclusions reversible as a matter of law." After consideration of the briefs, oral argument of counsel, the opinion of the Tax Court and the record as a whole, we hold that there was substantial evidence to support the Tax Court's findings and that the Tax Court did not err in holding petitioners liable for income tax deficiencies in the amount of $201,022.33. *Zeddies* v. *C.I.R.*, 7 Cir., 264 F. 2d 129, 126 (1959), cert. denied, 360 U.S. 910, rehearing denied, 361 U.S. 855.

Petitioners also contend that the Tax Court erred in finding that "a part of the deficiency is due to fraud" and assessing a fifty per cent penalty. Under Section 6653(b) of the Code, *supra* n.1, the fifty per cent penalty may be assessed against the entire deficiency, even though the finding of fraud relates only to part of the deficiency. The burden of proving fraud is on the Commissioner. *Paddock* v. *United States*, 2 Cir., 280 F. 2d 563, 565 (1960).

Civil fraud need not be proved beyond a reasonable doubt, but it must be established by clear and convincing evidence. *Spies* v. *United States*, 317 U.S. 492, 495 (1943);

Zeddies v. *C.I.R.*, 7 Cir., 264 F. 2d at 127; *Karnick* v. *Commissioner of Internal Revenue*, 6 Cir., 232 F. 2d 678, 681 (1956).

The question of fraud is one of fact and the Tax Court's finding is entitled to finality unless it is clearly erroneous. *Bodoglau* v. *Commissioner of Internal Revenue*, 7 Cir., 230 F. 2d 336, 341 (1956); Int. Rev. Code of 1954, §7482. We find convincing evidence in the record as a whole to support the finding of fraud. We hold that the Tax Court did not err in assessing a fifty per cent penalty on the entire tax deficiency. 37 T. C. at 752-754.

Petitioners further contend that the Tax Court twice abused its discretion in the trial of the case.

The Tax Court, over objection of petitioners, granted the Commissioner's motion for leave to file an amendment to his answer to petitioners' petition. The amendment alleged facts concerning an additional item which supported the Commissioner's determination of fraud. Petitioners contend that they were not given sufficient time to meet this allegation.

"The [Tax] Court may at any time, during the course of the trial on the merits grant a motion of either party to amend its pleadings to conform to the proof . . . ." Tax Court Rule 17(d). *C.I.R.* v. *Finley*, 10 Cir., 265 F. 2d 885, 888 (1959), held that this rule allowed amendment at any time before a final decision, and held that an amendment was proper even though made several months after the taking of testimony. In the present case, the amendment was filed *prior to trial*. We hold that the Tax Court's allowance of the Commission's motion to amend was a proper exercise of discretion and petitioners had sufficient opportunity to defend this additional allegation of fraud.

The second abuse of discretion asserted by petitioners was the Tax Court's denial of petitioners' motion for rehearing. An exercise of discretion by the Tax Court in denying a motion to reopen a case will not be reversed on appeal unless there is a showing of extraordinary circumstances. *ABC Realty Company* v. *C.I.R.*, 8 Cir., 295 F. 2d 98, 107 (1961). We have carefully examined petitioners' motion and the three accompanying affidavits. It is our conclusion that no circumstances are demonstrated which show an abuse of discretion by the Tax Court.

We have deemed it unnecessary to engage in a detailed statement of the evidence in this case, in view of our reference to the decision of the Tax Court. It is sufficient for us to say that based on our consideration of the record as a whole, with deference to the trier of fact in the determination of matters of credibility and weight to be assigned to various items of evidence, we are convinced that the deficiencies assessed and the finding of fraud have ample support in the record and must be affirmed. We find no prejudicial error therein.

The decision of the Tax Court is in all respects affirmed.

AFFIRMED.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
Chicago 10, Illinois

Monday, February 10, 1964
Before
Hon. JOHN S. HASTINGS, *Chief Judge*
Hon. ELMER J. SCHNACKENBERG, *Circuit Judge*
Hon. LUTHER M. SWYGERT, *Circuit Judge*

Charles Oran Mensik and Mary Mensik, *Petitioners*, vs. Commissioner of Internal Revenue, *Respondent.*	Petition for review of a decision of the Tax Court of the United States.
No. 14467	

This cause came on to be heard on the transcript of the record from the Tax Court of the United States and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that the decision of the Tax Court of the United States entered in this cause on February 21, 1963 be, and the same is hereby, Affirmed, in all respects in accordance with the opinion of this Court filed this day.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
Chicago, Illinois, 60610

Tuesday, March 17, 1964

Before

Hon. JOHN S. HASTINGS, *Chief Judge*
Hon. ELMER J. SCHNACKENBERG, *Circuit Judge*
Hon. LUTHER M. SWYGERT, *Circuit Judge*

Charles Oran Mensik and Mary Mensik, *Petitioners,*	Petition for review of a decision of the Tax Court of the United States.
No. 14167	
vs.	
Commissioner of Internal Revenue, *Respondent.*	

It Is Ordered by the Court that the petition for rehearing filed by petitioners herein be, and the same is hereby Denied.